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C O N F I D E N T I A L USNATO 3549

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SUBJECT: ECONADS: EXPERTS MEETING AT NATO, JULY 10-11, ON ECONOMIES
OF CZECHOSLAVAKIA GDR, AND HUNGARY

REF: USNATO 3474

SONOMIC DIRECTORATE HAS ISSUED ADDENEDM TO DUCUMENT AC/127-
D/514-ECONOMIC REVIEW OF EASTERN COUNTIES: CZECHOSLAVAKIA
(WHICH MISSION HAS ALREADY FORWARDED TO DEPARTMENT AND PRAGE,
WITH REQQ ST FOR COMMENT IN CONNECTION WITH SUBJECT MEETING).
ADDENDUMCONTAINS SUMMARY OF PAPER AS A WHOLE, PLUSE ADDITIONAL
CHAPTER ENTITLED"PROSPECTS FOR ECONOMIC CHANGES" AND AN
APPENDIX C ENTITLED "ECONOMIC INVOLVEMENT INDEVELOPMENT PRO-
JECTS IN THE CMEA AREA". WE ALSO ARE SENDING ADENDUM TO
DEPARTMENT AND PRAGUE FOR REVIEW. IN MEANTIME, TEXT OF SUMMARY
AND CHAPTER ON PROSPECTIVE ECONOMIC CHANGES IS SET FORTH BELOW:

BEGIN TEXT

CZECHOSLOVAKIA; THE ECONOMY SINCE 1971

SUMMARY

1. BY 1971 THE CZECHOLSLAVAKIA ECONCOMY HAD REGAINED
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STABILITY AFTE THE DISTURBANCES ON 1967-1969. THE RATE OF
ECONOMIC GROWTH HAS BEEN STEADY AND SLIGHTLY IN EXCESS OF THE
1971-1975 PLAN, ALTHOUGH IT REMAINS THE LOWEST AMONG THE EAST
EUROPEAN COUNTRIES OF THE WARSAW PACT.

2. CZECHOSLOVAKIA'S INDUSTRY, WHICH IS ONE OF THE MOST ADVANCED AMONG THE COUNTRIES OF THE WARSAW PACT, IS PARTICULARLY DEPENDENT ON FOREIGN TRADE SINCE A HIGH PROPORTION OF ITS FUEL AND RAW MATERIALS HAS TO BE IMPORTED AND, IN ADDITION, INTERNATIONAL MARKETS ARE ESSENTIAL IF ITS MANUFACTURED GOODS ARE TO ACHIEVE AND MAINTAIN MODERN TECHNOLOGICAL STANDARDS. THE RISE IN WORLD PRICES FOR FUELS AND RAW MATERIALS THEREFORE POSES SERIOUS PROBLEMS, SINCE IT HAS NOT BEEN MATCHED BY A COMMENSURATE RISE IN THE PRICES OF THE MANUFACTURED GOODS WHICH CZECHOSLOVAKIA EXPORTS.

3. AGRICULTURAL OUTPUT HAS INCREASED SUBSTANTIALLY AND CZECHOSLOVAKIA HAS BECOME VIRTUALLY SELF-SUFFICIENT IN LIVESTOCK PRODUCTS. GRAIN YIELDS HAVE BEEN WELL ABOVE PLAN, BUT IMPORTS OF ABOUT 1.5 MILLION TONS OF GRAIN A YEAR ARE STILL NECESSARY.

4. THE ECONOMY CONTINUES TO SUFFER FROM A SHORTAGE OF LABOUR AND POOR LABOUR MORALE, ALTHOUGH THE RISE IN LABOUR PRODUCTIVITY HAS BEEN ALMOST UP TO PLAN.

5. THE SHARE OF RESOURCES ABSORBED BY INVESTMENT PROGRAMMES HAS BEEN HIGHER THAN INTENDED, BUT WHILE THERE HAS BEEN OVERSPENDING ON MACHINERY THERE HAVE BEEN FAILURES AND DELAYS IN COMPLETING LARGE, IMPORTANT PROJECTS. A SUBSTANTIALLY INCREASED SHARE OF INVESTMENT HAS BEEN ALLOCATED TO THE FUEL AND POWER INDUSTRIES WHERE MORE CAPACITY IS STILL NEEDED.

6. THE RISE IN MONETARY INCOMES HAS BEEN KEEPING PACE WITH THE OVERALL RATE OF ECONOMIC EXPANSION AND IT APPEARS THAT IN GENERAL THE CONSUMER HAS RECEIVED A DUE SHARE OF THE BENEFITS FROM ECONOMIC GROWTH. RETAIL PRICES HAVE BEEN KEPT FAIRLY STABLE AND THE PARTY IS PLEDGED TO CONTINUE THIS UNTIL THE END OF 1975. CZECHOSLOVAKIA AND THE GDR HAVE THE HIGHEST LIVING STANDARDS AMONG THE COUNTRIES OF THE WARSAW PACT.

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7. ALTHOUGH CZECHOSLOVAKIA HAS BEEN CONDUCTING AN INCREASING SHARE OF HER FOREIGN TRADE WITH NON-COMMUNIST COUNTRIES, SHE REMAINS BEHIND ALL HER COMMUNIST PARTNERS, EXCEPT BULGARIA, IN THE PROPORTION OF TRADE WITH THE DEVELOPED WEST (26 PERCENT OF HER TURNOVER IN 1974). CZECHOSLOVAKIA HAS NO SIZEABLE HARD CURRENCY RESERVES ON WHICH SHE CAN DRAW AND AS HER DEFICITS WITH THE CONVERTIBLE CURRENCY AREA HAVE INCREASED SUBSTANTIALLY IN 1973-1974, AND THIS IS LIKELY TO CONTINUE, SHE MAY HAVE TO CHANGE HER POLICY ON THE USE OF WESTERN CREDITS WHICH IN THE PAST HAS BEEN ELUCTANT AND LIMITED. BECAUSE OF THE RISE IN WORLD MARKET PRICES, MEASURES HAVE BEEN TAKEN TO TIGHTEN CENTRAL CONTROL OVER IMPORTS FROM THE WEST AND, IN ADDITION PRODUCTION OF CERTAIN GOODS, E.G.

TEXTILES, WHICH REQUIRE HIGH-PRICED WESTERN INPUTS IS BEING REDUCED.

8. WITHIN CMEA CZECHOSLOVAKIA HAS A PARTICULAR INTEREST IN ENSURING SUPPLIES OF FUEL, ENERGY AND RAW MATERIALS EVEN THOUGH THE PROGRESSIVE REVISION OF PRICES FROM 1975 ONWARDS (A YEAR EARLIER THAN EXPECTED) WILL RESULT IN A DETERIORATION OF HER TRADING POSITION IN RELATION TO THE MAIN SUPPLIERS, PARTICULARLY THE SOVIET UNION. IT IS POSSIBLE THAT SOME OF HER PRESENT EXPORTS WHICH EARN HARD CURRENCY MAY HAVE TO BE DIVERTED TO THE SOVIET MARKET, ALTHOUGH IN ORDER TO MAINTAIN TECHNOLOGICAL ADVANCE AND HER COMPETITIVE POSITION AS AN EXPORTER A GREATER INVOLVEMENT IN TRADE WITH THE WEST IS LIKELY TO BECOME A NECESSITY.

9. WE ESTIMATE THAT EXPENDITURES ON DEFENCE HAVE BEEN ABSORBING ABOUT 4 PERCENT OF CZECHOSLOVAKIA'S GNP EACH YEAR AND THAT THE GROWTH OF THESE EXPENDITURES HAS BEEN MAINTAINED AT ABOUT THE SAME RATE AS THE OVERALL GROWTH OF THE ECONOMY.

10. THE PROSPECTS FOR ECONOMIC REFORMS IN CZECHOSLOVAKIA APPEAR REMOTE AND A SCHEDULED REFORM OF INTERNAL PRICES, ALTHOUGH INCREASINGLY NECESSARY, IS LIKELY TO PROVE DIFFICULT.

X. PROSPECTS FOR ECONOMIC CHANGES

59. UNDERSTANDABLY ENOUGH, IN VIEW OF THE SOVIET INTERVENTION IN 1968-1969, THE NEED FOR ECONOMIC CHANGES, WHILE CONFIDENTIAL

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BY NO MEANS TABOO, IS A SUBJECT WHICH IS TREATED WITH CONSIDERABLE RETICENCE IN CZECHOSLOVAKIA'S PUBLICATIONS. THE PROBLEMS AND SHORTCOMINGS OF THE ECONOMY ARE FRANKLY ADMITTED BUT IT IS DIFFICULT TO DISCOVER THAT, IF ANY, MEASURES ARE LIKELY TO BE TAKEN IN THE NEAR FUTURE TO SECURE IMPROVEMENTS. EVEN WHEN PROGRAMMES ARE ALREADY IN PROGRESS, FOR INSTANCE IN THE NEW WAGE SYSTEM WHICH HAS ALREADY GRADUALLY INTRODUCED SINCE 1972, NO COMPREHENSIBLE ACCOUNT OF THE MAIN TRENDS AND INTENTIONS IS EASILY AVAILABLE.

60. BECAUSE OF THE GENERALLY CAUTIOUS ATTITUDE OF THE CZECHOSLOVAKIAN LEADERSHIP, AND THE INHIBITING INFLUENCE OF THE SOVIET UNION, THE PROSPECTS FOR ANY MAJOR ECONOMIC CHANGES HAVE SEEMED REMOTE. THE SECTOR IN WHICH GRADUAL MODIFICATION HAS BEEN IN PROGRESS WAS FOREIGN TRADE WHERE ENTERPRISES PRODUCING GOODS FOR EXPORT APPEAR TO HAVE GAINED MORE AUTONOMY, WITH SOME FIFTY OF THEM ENGAGING DIRECTLY IN FOREIGN TRADE TRANSACTIONS IN 1972. HOWEVER, WITH THE DIFFICULTIES CREATED BY THE RISE IN WORLD PRICES FROM 1973 ONWARD THIS TREND HAS BEEN REVERSED AND CENTRAL CONTROL TIGHTENED (SEE PARAGRAPH 58 ABOVE).

61. TOWARDS THE END OF 1974 THERE WAS EVIDENCE OF A DEBATE ON ECONOMIC POLICY AMONG THE LEADERSHIP IN WHICH ADVOCATES OF REFORM, INCLUDING THE SLOVAK DEPUTY PRIME MINISTER DURKOVIC, ARGUED THE NEED FOR GREATER DELEGATION OF RESPONSIBILITY TO MIDDLE-LEVEL MANAGEMENT IN ORDER TO SECURE IMPROVEMENTS IN PRODUCTION QUALITY AND LOWERING OF PRODUCTION COSTS. THESE

ARGUMENTS APPAEAR TO HAVE BEEN INEFFECTIVE.

62. A MAJOR OUTSTANDING QUESTION IS THE FEASIBILITY OF AN INTERNAL PRICE REFORM, WHICH HAS LONG BEEN SCHEDULED FOR IMPLEMENTATION AT THE BEGINNING OF 1976. THE NEED FOR THIS IS PRSUMABLY BECOMING MORE AND MORE URGENT, SINCE THE RISE IN COSTS OF MATERIALS IMPORTED FROM THE WEST ALREDY NECESSITATED A LARGE BUDGETARY SUBSIDY IN 1974 (SE PARAPGRH 43 ABOVE). IN 1975 THERE ARE ALSO HIGHER COSTS FOR MATERIALS IMPORTED FROM CMEA COUNTRIES (SEE PARAGRAPH 54). HOWEVER, THERE WILL CERTAINLY BE MAJOR PROBLEMS INEFFECTING A PRIVE REVISION WHICH TAKES DUE ACCOUNTY OF THESE RECENT RAPID CHANES, AND
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ALSO THE FURTHER RISES IN CMEA PRICES WHICH ARE SCHEDULED TOTAKE PLACE EACH YEAR
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